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C O N F I D E N T I A L SECTION 01 OF 03 BAKU 000566

SIPDIS

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TAGS: PGOV PREL ENRG AJ TX TK
SUBJECT: AZERBAIJAN: SOCAR TELLS SE GRAY EVERYONE WANTS
GOAJ GAS

Classified By: Ambassador Anne E. Derse, reasons 1.4 (b,d)

¶1. (C) SUMMARY. SOCAR President Rovnaq Abdullayev told a USG delegation on June 2 that in addition to competition among the Nabucco, TGI and TAP pipeline projects for Shah Deniz Phase Two gas, Turkey, Israel, Iran and Russia have each individually notified SOCAR that they wish to purchase all of Shah Deniz Phase Two gas. Azerbaijan is unlikely to take the offers of either Israel, Iran or Russia for SD2 gas, although if Russia were to link SD2 sales to solving N-K the GOAJ would be faced with a tough decision. Absent that development, the competition for SD2 is still between Nabucco and TGI, since despite SOCAR's wishes it does not seem likely that SD2 will have enough to fill TGI and to start Nabucco; a key question in this regard is how much (or more accurately how little) SD2 gas will induce Turkey to open itself up for transit of the remaining SD2 volumes. Abdullayev recognizes that Turkmen gas will be needed to help secure new Caspian gas sales to Europe. He also underscored that while while the GOAJ would honor its existing PSAs, it sought a way to transit expected volumes of Kazakh oil that would not lessen its own ownership of the BTC pipeline. END SUMMARY

¶2. (C) On June 2, a USG delegation headed by Special Envoy for Eurasian Energy C. Boyden Gray and including Eurasian Energy Coordinator Ambassador Steve Mann, Charge D'Affaires to Turkmenistan Ambassador Richard Hoagland, Ambassador Derse, EEB Energy Officer Larry Wright and EnergyOff (notetaker) met with SOCAR President Rovnaq Abdullayev, Marketing VP Elshad Nassirov, and Development Manager Vaqif Aliyev.

SD2: NABUCCO, TAP, TGI WANT IT...

¶3. (C) Abdullayev said in a recent meeting Nabucco partner RWE had told SOCAR it needed to purchase at least 15.5 billion cubic meters annually (bcm/a) from the Shah Deniz Phase Two (SD2) for the pipeline's first phase, "or else the project won't go ahead." He said when SOCAR had talked to OMV a year ago, it had sought a minimum of 5 bcm/a for Nabucco. With expected annual SD2 production of approximately 13 bcm/a, and with some of that to be earmarked for Georgia and Azerbaijan, SD2 couldn't meet this request even if it wanted to. He added that TGI pipeline was seeking a minimum of 5 bcm/a from SD2 and TAP had a 6 bcm/a minimum request, meaning that among just these three pipeline projects aggregate demand was over 26 bcm/a.

...TURKEY WANTS IT ALL...

¶4. (C) Additionally, Botas has told SOCAR it wants to buy

all of SD2 production for domestic Turkish consumption, but would be satisfied with a minimum of 8 bcm/a. Without this 8 bcm/a, Abdullayev understood that the GOT would not allow transit of Azerbaijani gas for European markets. However, he said if Azerbaijan did sell 8 bcm/a to Turkey, it would have only 2 bcm/a left for European markets (assuming that 3 bcm/a of SD2 would be for Azerbaijan and Georgian use). Abdullayev said he planned to meet with the Shah Deniz Consortium to find out the most up-to-date information on expected SD2 production. His hope was that if the GOT could be satisfied with 5 bcm/a, perhaps there would be 10 bcm/a of SD2 left to for two other pipeline projects. Speaking more generally, Abdullayev said that, given an approximately USD 15 billion expense for SD2 development, SOCAR needed to review the overall Shah Deniz development project "to see if it is economical."

...AS DOES RUSSIA ISRAEL, IRAN

¶5. (C) Abdullayev said that in a recent meeting Israeli Minister of National Infrastructure Ben Elizer (in Baku for the Caspian Oil & Gas Show), said Israel wanted to buy all of SD2 production at market prices. Additionally, Abdullayev said that during a meeting earlier that day, Gazprom Chairman Alexei Miller told him that Russia too sought to buy all of SD2 volumes at market prices. And, a few days prior an official Iranian delegation informed SOCAR that Iran too wished to buy all of Shah Deniz Phase Two volumes. Smiling broadly, Abdullayev summed it up by saying that in the last three days, Turkey, Iran, Israel and Russia had each informed SOCAR that it wished to buy all of SD2 volumes.

TURKMENISTAN

¶6. (C) Abdullayev said Turkmen gas flowing to Azerbaijan would significantly enhance SOCAR's ability to support the various pipeline projects, agreeing with Ambassador Mann that timing is the issue. Saying that SOCAR had laid 500 kilometers of pipeline in the Caspian in the previous year, he added that building the 380 kilometers needed to hook up with Turkmenistan would be easy. As such, he agreed with Ambassador Derse that the main obstacles in the way of a GOTX-GOAJ interconnector are political, not technical, although he said that given ACG and SD infrastructure design, any interconnector would have to connect to the Azerbaijani coast. Overall bilateral delimitation is not important, since the pipe would run east-west while the delimitation line is north-south. If GOTX volumes were to come west, new gas pipelines to Erzurum would be needed, although everything depended on the volume of Turkmen gas coming west. Echoing President Aliyev's sentiments, Abdullayev said that Turkmenistan, not Azerbaijan must be the initiator of any deal to interconnect their respective offshore infrastructures in order to transit GOTX gas west. Mann responded that while it is true that, as Abdullayev said, "Azerbaijan doesn't need GOTX gas," it is good for Azerbaijan to have productive relations with Turkmenistan. All agreed that strengthening GOTX-GOAJ energy sector cooperation should be done with as little publicity as possible. In response to Mann's question, Abdullayev said that SOCAR would need take or pay volume commitments from Turkmenistan before building any interconnector or pipeline for GOTX gas, to which SE Gray responded that they would work on seeking such a commitment when they traveled on to Ashgabat after this leg of the visit.

¶7. (C) In response to SE Gray's question about what he could do to advance Turkmenistan-Azerbaijan energy cooperation, Abdullayev said that the ball was in Turkmenistan's court - he had briefed the head of Turkmenistan,s State Agency For Hydrocarbon Resources Baimurat Muradov on Azerbaijani proposals for joint development during his recent visit to

Baku, laying out SOCAR's vision of providing GOAJ energy infrastructure to the GOTX and jointly developing the Sardar-Kapaz offshore field. Now Azerbaijan was waiting for feedback from Turkmenistan.

KAZAKH OIL TRANSIT

¶8. (C) Ambassador Mann encouraged Azerbaijan to be an effective partner in moving Kazakh oil volumes to market. Abdullayev said that would be no problem, as Azerbaijan had rail, ships and pipelines available to do so. Delays were the Kazakhs' fault, but SOCAR would be discussing commercial principles later in the week with Kazakh interlocutors. Azerbaijan planned to eventually transit 20 million tons annually by rail, 20 million tons annually by BTC, and 30 million tons annually by a new pipeline, for a maximum annual capacity of 70 million tons.

¶9. (C) In this regard, Mann expressed USG full support for BTC expansion to 1.2 mmbd. Abdullayev said he wasn't against expansion, but didn't want Azerbaijan to lose ownership share as Kazakh oil volumes through BTC increased, as would happen under the terms of the current PSA. Mann countered that the current PSA was a good one and should be honored, with Abdullayev saying that Azerbaijan always honors its contracts. However, under the existing PSA after ZBD (zero balance date, 2024, when the BTC Consortium loses ownership of the pipeline), SOCAR ownership would decrease from 85 percent to 48 percent if Kazakh transit volumes were to increase to expected levels, and this was something that "Azerbaijani future generations would blame us for." Mann countered that Azerbaijan's future generations would say that SOCAR was commercially reliable, repeating that the USG wished for BTC expansion, which was desirable for both Azerbaijan and the US, and looked to SOCAR for support. Abdullayev said that SOCAR fully supports BTC expansion and will adhere to its contacts, maintaining its reputation as the most commercially reliable country in the region.

10.(C) COMMENT: Given that Azerbaijan seeks to market its gas for primarily geostrategic vice commercial reasons, it is unlikely to take the offers of either Israel, Iran or Russia

for SD2 gas, although if Russia were to link SD2 sales to Russian support for solving N-K the GOAJ would be faced with a tough decision. Absent that development, the competition for SD2 is still between Nabucco and TGI, since despite SOCAR's wishes it does not seem likely that SD2 will have enough to fill TGI and to start Nabucco. A key question in this regard is how much (or more accurately how little) SD2 gas will induce Turkey to open itself up for transit of the remaining SD2 volumes.

¶11. (U) SE Gray and Ambassador Mann have cleared this cable.
DERSE